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### Introduction

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## **Encyclopedia Entry [Iraq, POLITICAL ECONOMY]**

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### **I. Introduction: The state, oil, and war.**

Three themes have influenced the shape and the direction of Iraq's economy since the foundation of the modern Iraqi state as a League of Nations' mandate in 1920: the state, oil, and war. While these themes appear to be dominant, they should not be understood as isolated from other international, regional and national political and economic forces.

The state's capacity to enforce law and order (regardless of the nature of the political system) has always been a major factor in shaping the nature of the Iraqi national economy. The increased capacity of the state that proceeded the Ottoman Empire accelerated the emergence of a national economy out of fragmented and isolated local economies and the integration into an international world market. The state's influence became most obvious with the nationalization of the oil industry in 1972 and the emergence of a state-commanded economy that slowly gave way to economic liberalization in the 1980s. The weakening of the state (due to wars and sanctions) became visible in the 1990s, and most visible after the second Gulf War and the US-led invasion of 2003. The decline of state capacity allowed the formation and consequent consolidation of smuggling and criminal networks that operate within the economy.

For the past three decades, Iraq's economy has been heavily influenced by war. The eight-year interstate war with Iran (1980-1988) resulted in a heavy financial debt and subjected the economic priorities to the war efforts. The economic damages caused by the war were compounded by the subsequent first Gulf War (1991), the international comprehensive sanctions (1990-2003), the second Gulf War (2003), the civil war (2006-7), the emergence of the Islamic State (since 2014), and the general political instability since 2003.

The most recent episode in Iraq's political economy was initiated by the US-led occupation in 2003 and its effort at Iraqi state-building. Upon the occupation of Iraq the US initiated ambitious state-building efforts that faced multiple challenges leading to a difficult and slow process of reconstruction. State institutions, public infrastructure and consequently the economy suffered during this decade from multiple episodes of violence, management inefficiencies, allegations of corruption, and political instability. While Iraq seems to be making a recovery after decades of strenuous economic and political circumstances, a restoration of a state of normalcy and reaching its prosperous potential are yet to be achieved.

### **II. Late Ottoman through the Monarchical period (1831-1958)**

The period from the late Ottoman (1831-1914) through the British occupation (1914-1920) and Mandate (1920-1932), and the Monarchy (1932-1958) witnessed radical changes in terms of the emergence of a national economy, integration into the world market, discovery of oil in Iraq, and the emergence of new wealth that altered the social and political landscapes of the country.

#### **i. Fragmented, subsistence economies.**

Prior to the establishment of the modern Iraqi state under the British League of Nations' mandate in 1920, Iraq was part of the Ottoman Empire since 1550. Ottoman control was constantly challenged and was finally stabilized in 1831 and lasted through the start of British invasion in 1914. Under the Ottomans, and due to a number of reasons, the country was composed of "plural, relatively isolated, and often virtually autonomous city-states and tribal confederations".<sup>1</sup> During this period, Iraq's economy was fragmented along the different communities and had generally kept subsistence

economies that were not interdependent.<sup>2</sup> This was partly due to the poor communications and transportation infrastructure, wherein major Iraqi cities were better linked to other major (non-Iraqi) economic centers, including in India and Syria, then to Iraqi towns.<sup>3</sup> The Ottomans would attempt to centralize the state control and subsequently bring about a form of a national economy, but it was not until the British occupied Iraq that the process of change became expedited leading to many intended and un-intended economic, social, and political consequences.

## **ii. Integration into the international market—Ottoman beginnings**

British and monarchical policies in Iraq helped expedite the emergence of a national economy and the integration into an international market. However, it is worth noting that prior to the British occupation of Iraq in 1914, the Iraqi economy was already slowly becoming integrated into a British imperial market in the course of the nineteenth and twentieth centuries. One critical event was the opening of the Suez Canal in 1869, which combined with “[t]he gradual introduction of steam navigation on the Tigris and Euphrates rivers enabled Iraq to become an exporter of grain, mostly to the Gulf and India.” While Iraq was still under Ottoman control, the volume and value of its grain exports increased a sixty-fold between 1867 and 1913.<sup>4</sup>

In an effort to increase the state’s tax collection abilities, the Ottomans, under Midhat Pasha (1869-72), tried to introduce the Ottoman Land Code of 1858 to Iraq. The Code was meant to organize and codify forms of land ownership in order to institute the state’s ability to impose and collect taxes. Up to this point, and for a while to come, land in Iraq was generally held collectively by tribes. A tribe’s land holding was dependent on its ability to defend it against other tribes. In effect, there were no private property mechanisms to enforce the new legal codes. Upon the introduction of land reforms, Ottoman land deeds were issued based on hasty evidence, and only those who understood the long-term significance of this law obtained land deeds and thus became large landowners overnight. The inability of the state to enforce private property rights, and collect taxes, defied the main purpose of introducing the Code and subsequently led to the termination of issuing land ownership deeds in 1881.

The gradual integration into the world market, the introduction of private property, and the Ottoman’s state attempts at organizing private ownership in order to increase its tax collection abilities, introduced an inevitable conflict of interests among the state, tribal leaders and tribesmen. Many tribal leaders were transformed by the new Code into big landowners, and their tribesmen, who were still expected to defend the land against the Ottoman state and other tribes, were at the same time being slowly transformed from fighters defending tribal lands, to farmers growing crops for export. These tensions, if they continued, would have led to the decline of the institution of the tribe as a sociopolitical and economic unit according to Hana Batatu.<sup>5</sup>

## **iii. Mandate and Monarchy: large land ownership and mass migrations**

British policies to ensure political neutrality and/ or support among the population Iraq had immense economic consequences on the country that mainly affected the structure of land holdings and the demographic landscape. Unlike the Ottomans, the British were able to secure private property rights, and had granted lands to tribal leaders in exchange for political support/ neutrality. This policy continued throughout the mandate (1920-1932) and monarchy period (1932-1958) and, with combination of other policies, resulted in the creation of concentrated large land ownerships in the hands of few families.<sup>6</sup> These lands became cultivated for the profit of landowners with the help of 1926 and 1932 laws that encouraged the use of irrigation pumps and continuous cultivation of land. These economic and legal incentives to cultivate the land for financial profit occurred within a context wherein the new large landlords had no former knowledge of land cultivation but demanded constant production from the farmers. As a result of that, cultivation used wasteful agricultural methods that led to the significant decline of land productivity over the course of thirty years.

The 1933 Law Governing the Rights and Duties of Cultivators, put extreme financial burdens on the land cultivators that included the prohibition of leaving the land if the cultivator was in debt. Adding to the poverty and difficult living conditions of Iraqi cultivators, the implementation of the 1933 Law led to the initiation of massive escapes from the land, especially in the south where most of the cultivate lands were located, to Baghdad and its outskirts forming the future working class of the city.<sup>7</sup>

#### **iv. A growing economic and state infrastructure**

Despite land and tax policies that have led to the economic hardship for a significant number of the population and the depletion of agricultural land (among other negative political and social consequences), the British and monarchical policies in Iraq resulted in the consolidation of state power which allowed the emergence of a previously non-existing national economy.

Due to different reasons and motivations, the monarchy “added to the material factors making for a consolidated and more powerful state”.. for example, the threefold increase in “gravel or hard surface roads” between 1944 and 1955 mostly in the middle and northern parts of the country.<sup>8</sup> Also, the “administrative machine and security apparatus of the state grew larger.” Dams and barrages were “erected in the fifties on the Diyālah, the Lesser Zāb, the upper Euphrates near Rāmadī, and the upper Tigris near Sāmarrā’.”<sup>9</sup> thus improving the water supply for irrigation and protecting Baghdad and the (mostly agricultural) south from floods.

Under the monarchy, British domination of financial institutions, although not economic influence, was diminishing as a result of the Iraqi governments creation of its own institutions: the Agricultural Bank in 1936; the Rafidain Bank in 1941; the Industrial Bank in 1946; and the Central Bank in 1947. Local businessmen created financial houses as well. The railways became a national property in 1936, and under full Iraqi control in 1952. At the same time, British companies remained the main beneficiaries of Iraqi trade providing, for example, 31.2 percent of Iraq’s imports between 1952-1958.<sup>10</sup>

#### **v. The Shift to a Rentier Economy**

This surge of infrastructure construction (late 40s, 50s) was animated by the increased flow of cash to the treasury from oil revenues. This increased flow was due to two reasons—the oil companies’ attempt to punish Iran for nationalizing its oil industry in 1951; and their desire to help improve the position of the Iraqi monarchy nationally. Iraqi oil revenues went from 5,286,000 Iraqi Dinars in 1950 (15.7 percent of the total national revenue) to 13,295,000 ID in 1951, and to 79,888,000 ID in 1958 (61.7 percent of the total national revenue).<sup>11</sup> The surge of oil rents in the hands of the state in the 1950s, which enabled the state to perform various projects and consolidate its presence, has since then become the norm. Since that date Iraq become a country with a rentier economy and a rentier state—deriving most of the national income from non-productive economic activities, in this case, oil revenues.

Prior to the dependency on oil, Iraq’s agriculture provided the majority of the country’s GDP. In 1911 it composed 44.3 percent of the total national revenue, and between 20 and 25 percent in the 1920s. As Iraq’s oil revenues started increasing in the 1930s, the percentage of agricultural revenues (rather than the actual volume of production) dropped reaching to a range between 17 and 8 percent for the decade spanning from 1934 to 1945. The surge of oil revenues in the 1950s lead to a major relative drop in agricultural contribution to the national income wherein it reached 8.1 percent in 1951 and 1.7 percent in 1958.<sup>12</sup>

The increase in national wealth post 1920 through 1958, thanks mainly to oil and an increasingly consolidated state apparatus, was also accompanied by an increase in social inequalities. Most of the wealth was concentrated within a small number of families, and most of the generated wealth went to foreign oil and trade companies. British firms, even after the creation of Iraqi financial institutions, were still the major beneficiaries of economic activities in Iraq.<sup>13</sup> These vast inequalities became a major factor in the mobilization of various protests and the subsequent military take-over of the state apparatus in 1958—an event that led to the abolishment of the monarchy and the establishment of an Iraqi republic.

### **III. 1970s: Nationalization of the Oil Industry and the Developmental State**

The republican regime that was instated in 1958 remained unstable and suffered from multiple coups. At the same time, it ushered the start of a state-commanded economy with the sweeping nationalization in 1964 by the Iraqi President Abd al-Salam Arif. The Ba'thist coup of 1968 ushered a more stable era in which Saddam Hussein was president of Iraq from 1979 through the US-led invasion in 2003. Economically, the first decade of the Ba'thist era (1970s) witnessed two major events: the nationalization of the oil industry, and the emergence of the developmental welfare state.

#### **i. From the Turkish Petroleum Company to the Ministry of Oil**

Iraq's oil industry started with the establishment of the Iraq Petroleum Company (IPC) in 1912 as the Turkish Petroleum Company. The latter was owned by Deutsche Bank, Royal Dutch/ Shell, a British bank that was based in Turkey and called the National Bank of Turkey, and the Arminian businessman Calouste Gulbenkian—who also held shares in the British government-controlled Anglo-Persian Oil Company.<sup>14</sup> But Iraqi oil made its big appearance in 1929, when a British, Dutch and American joint oil expedition started drilling near the town of Kirkuk, “from a well known as Baba Gurgur Number 1—in which the drill bit had barely passed fifteen hundred feet—that a great roar was heard, reverberating across the desert. It was followed by a powerful gusher that reached fifty feet above the derrick, carrying in it rocks from the bottom of the whole... Finally, after eight and a half days, the well was brought under control. It had flowed, until capped, at ninety-five thousand barrels per day.”<sup>15</sup> This signaled the start of Iraq becoming one of the major international oil producers. In the same year, the ICP was renamed as the Iraq Petroleum Company that was owned by a consortium of American oil companies (New East Development Corporation), the Anglo-Persian Oil Company, Royal Dutch/ Shell, Compagnie Française des Pétroles and Gulbenkian.

In 1960 the Iraqi capital, Baghdad, witnessed the founding of Organization of the Petroleum Exporting Countries (OPEC) of which Iraq was founding member. After the nationalization of the oil industry in 1972, the holdings of the IPC were transferred to the Iraq National Oil Company (INOC), which was established in 1964. In 1987, INOC was dissolved and merged into the Ministry of Oil. Under the new structure, oil exploration and production, transport and refineries were managed by 14 operating companies reporting to the ministry, while marketing activities fell under the State Oil Marketing Organization (SOMO).<sup>16</sup>

#### **ii. Nationalization of oil and the initiation of a developmental state based on a rentier economy**

The first Iraqi president, Abdel Karim Qasim attempted unsuccessfully to nationalize the oil industry. Law no. 80 of 1961 annulled concessions to oil companies in areas that were not under exploitation, but this law never took effect.<sup>17</sup> On June 1<sup>st</sup>, 1972 the Iraqi government nationalized the IPC – a move, along with termination of concessions to oil companies in other major oil producing countries (Iran in 1951, Kuwait in 1976, Venezuela in 1976, and Saudi Arabia in 1980) “would mark the demise of the twentieth century concessional arrangements that had begun... in 1901.”<sup>18</sup>

The nationalization of oil led to a dramatic increase in the oil rent's percentage of the GDP which increased steadily and dramatically reaching the highest ratio to date of 82.5 percent of the GDP in 1979.<sup>19</sup> This ratio was not sustained during the following decades which witnessed what is known as the oil glut in the 1980s, and the reduced capacity to produce and export oil due to wars and sanctions in the following two decades.

The 1970s witnessed the rise of a developmental welfare state in Iraq that relied mostly on oil revenues for its projects. This decade witnessed the reversal of many land laws to the benefit of farmers, abolished large private ownership of agricultural lands, introduced universal public healthcare and education that reached villages as well as cities, expanded the electrical infrastructure, introduced policies to encourage modern industrial agriculture, subsidized basic food staples, and increased the wages of public employees.<sup>20</sup> These improvements were reflected in the significant increase in the average life expectancy in Iraq. An Iraqi individual was expected to live on average until the age of 48 in 1960 (regional average for the MENA was 46.7). By 1977 the average went to 61 years old in Iraq, and 56.9 years old in MENA.<sup>21</sup>

During this decade Iraq initiated an industrial development policy, including import substitution, food-processing industries, the expansion of cement and building supplies industry, and developing petroleum refining and natural gas processing. There was also a shift towards heavy industry and a diversification away from oil.<sup>22</sup>

In 1975, Iraq signed the Algiers agreement with Iran, which settled a borders' dispute and ended Iranian support to the Kurdish militias in Iraqi Kurdistan. This partly meant that economic development plans, including the modernization of the oil and other industries, were freed from counter-insurgency military expenditures and helping Iraq become the second largest OPEC oil producer/ exporter by 1979.<sup>23</sup> By the end of the 1970s and in the 1980s Iraq's ranking for per-capita GDP among the middle and high-middle income countries reaching up to USD 3,346 (constant 2010 USD) in 1980.<sup>24</sup>

#### **IV. 1980s: War Economy and Debt**

The Iran-Iraq war (1980-1988) had a devastating effect on the Iraqi economy, and had, at the same time, transformed many aspects of it. The war was a military stalemate, but the economy that was subjected to it, and fed upon it, was transformed into new directions. Subjecting the economy to war efforts meant that development and welfare state-sponsored projects had to decline in favor for military expenditures. Another major outcome of the war was the emergence of a huge debt. While obtaining data on the economy and social life in Iraq during the Ba'thist period was difficult, the 1980s were a particularly difficult decade in this regard due to the state's guarding of this information during war time.

##### **i. The economic impact of oil and war**

The industrial and developmental projects of the 1970s were reduced in the 1980s due to the war with Iran, and have not since then recovered. Agriculture also suffered—where governmental financial support to the sector dropped from 18 percent of total government expenditures in 1976, to less than 10 per cent in 1980 and continued to decline during the war.<sup>25</sup>

Until the start of the Iran-Iraq war, Iraq was free of debt and had foreign reserves of 35 billion USD by 1980. The war quickly reversed this trend. It is estimated that Iraq acquired between 65 and 85 billion USD in debt for military assistance, development finance, and export guarantees: 35 to 45 billion USD to western creditors, and another 30 to 40 billion in assistance from the Gulf states.<sup>26</sup>

## **ii. Economic liberalization**

The reduced oil revenue and increasing debt led the state to initiate an economic liberalization campaign in the second half of the decade. One important consequence was a massive privatization campaign of state-owned factories. Another development was, in contrast to the policies pursued in the 1970s, new policies and regulations that weakened labor were introduced such as the lifting of minimum wage regulations and abolishing labor unions.<sup>27</sup> At the same time, due to the universal military conscription and sending many young men to the war front, a labor shortage took place during these years. This led to large-scale import of labor mostly from Egypt and Sudan. The majority of those workers would leave Iraq soon after the 1990 Iraqi invasion of Kuwait.<sup>28</sup> A third significant development was the emergence of contractors, among concentrated number of families, who carried government projects with funds that came from oil rent or foreign aid. In a speech regarding the size of this new wealth and what is expected from its owners, Saddam Hussein gave a glimpse into this phenomenon: "You know that there was only a handful of contractors before the revolution [the 1968 coup]... Now, this contractor owns not thousands [of Iraq dinars] but millions.... I was informed that he had donated only a pittance. He did not ask himself, 'Where did I get this fortune? Isn't it thanks to these new circumstances?'"<sup>29</sup>

## **V. 1990s: wars, international sanctions, and the Oil-for-Food Programme.**

By the end of the Iran-Iraq war in August 1989, Iraq was immersed in debt, suffered from destruction to its infrastructure (including that of oil), and a reversal of many of the welfare and developmental projects. Within a year of the war's end, Iraq invaded and occupied its neighboring country, Kuwait. This event led to the first Gulf War of 1991 and the introduction of comprehensive economic sanctions by United Nations Security Council Resolution 661 that would last until the fall of the regime in 2003 and would put the economy into a severe state of weakness.

### **i. First Gulf War: destruction and economic sanctions.**

The economic devastation incurred on Iraq during the 1980s due to the war, debt, and declining oil prices can arguably be considered a main trigger for the 1991 Gulf War. After the end of the war with Iran, Iraq wanted the Gulf countries (mainly Kuwait and Saudi Arabia) to forgive loans incurred during the war. It also accused Kuwait and the United Arab Emirates of exceeding their oil production quotas and thus driving down the international price of oil. This tension escalated when Iraq accused Kuwait of stealing oil from the Rumailia oilfields, which are located at a disputed border between the two countries. On August 2<sup>nd</sup> 1990, Iraq invaded and annexed Kuwait. The Iraqi occupation led to the 1991 Gulf War and the international comprehensive sanctions, both of which aimed to end this occupation and led to Iraqi withdrawal February 25 1991.

The Gulf War have caused damage to the infrastructure, including transportation, communications, water treatment and purification plants, sewage systems, and electricity. This was in addition to damages sustained during the war with Iran to the civilian infrastructure and oil facilities. Post-war reconstruction, however, was not possible due to the international comprehensive sanctions. The sanctions were first put in place to force Iraqi withdrawal from Kuwait, but were later extended under new conditions related to Iraq's weapons of mass destruction.

The sanctions froze all Iraqi assets abroad and put a complete halt on all trade in and out of Iraq except for food and medicine. However, because of the inability to generate income, mainly through oil sales, Iraq was not able to import sufficient amounts of the permitted items. This, in addition to the destruction of the infrastructure, led to a humanitarian crisis during the early years of the sanctions.

The scarce availability of medication, vaccines, food staples particularly animal protein, and the deteriorating water, sewage and electrical infrastructures led to the spread of malnutrition among

children and infants, and the emergences of epidemics that were eliminated in Iraq during the 1970s and 1980s. A famine situation was avoided due to the government's introduction of an efficient rationing system. The caloric availability prior to 1991 was 120 percent of the standard requirements, the rationing system, which was lacking in animal protein, was able to provide 53 percent of the 1987-89 food energy availability but this figure would drop to 34 percent by 1994. Another response to the scarcity of food was the encouragement of agricultural production, but in the absence of machinery, spare parts, pesticides, fertilizers, and a functioning irrigation system, this policy failed and led to the creation of more problems such as land salinization and the spread of malaria along rice fields.<sup>30 31</sup>

## **ii. The Oil-for-Food Programme: scope and benefits**

Upon a growing humanitarian crisis, Iraq was allowed to sell limited amount of oil within the terms of the Oil-For-Food Programme (UNSC resolution 986 of the year 1995) which were implemented at the end of 1996 and continued through the remaining years of the sanctions. The terms of OFF were renewable every six months by a UNSC resolution after the review and approval of Iraq's compliance and OFF's performance by the Sanctions Committee ("the 661 Committee" created by UNSCR 661). The period between two reviews was known as a "Phase". Iraq was allowed to sell a specified amount of oil in each phase. The money generated through those sales was to be deposited in a UN escrow account and used to purchase food stuffs and humanitarian goods. Contracts for oil sales and the purchase of food and humanitarian goods had to be approved by the 661 Committee. Under OFF Iraq sold USD 64.2 billion worth of crude oil.<sup>32</sup>

OFF was successful, in combination with the government rationing programme, in avoiding a major humanitarian situation in Iraq. At the same time, it did not lift the sanctions' limitations on importing sufficient material necessary for the post-war reconstruction and/ or achieving economic sufficiency. For example, according to a 2001 UN Secretary-General report, Iraq's requests for purchasing goods for its agricultural sector were mostly put on hold by the 661 Committee.<sup>33</sup> By 2002 Iraq imported between 80 and 100 percent of its food staples through OFF. But it remained self-sufficient in fruits and vegetables.<sup>34</sup>

After achieving a position among the middle-income and high-middle income countries in the 1970s and 1980s, Iraq's per capita GDP dropped significantly in the 1990s due to the sanctions, reaching a low of USD 1,428 (constant 2010 USD) in 1991— dropping under the average for middle-income countries. Iraq would recover its position of having higher per capita GDP than the average for middle income countries during the OFF years, reaching a high of USD 4,379 (constant 2010 USD) in 1999.<sup>35</sup> At the same time, the average of life expectancy continued to rise in the 1990s. Despite a drop in the early 1980s, most likely due to the war with Iran, it continued to rise following a regional trend and reaching up to 69 years old in 1998—which was equal to the regional average.<sup>36</sup>

OFF revenues were also used to pay compensation for claims made for reparations of damages by Kuwait during the Iraqi invasion and occupation of 1990. 30 percent of oil sales under OFF were dedicated to pay such claims that were authorized by the United Nations Compensation Commission (UNCC). This was reduced to 24 percent in December 2000.<sup>37</sup>

## **iii. OFF controversies**

OFF was surrounded with controversies of corruption as Iraq was able through the manipulation of the programme to general USD 1.5 billion in kickbacks on humanitarian goods contracts and 229 million USD in illicit payments on oil contracts. It also cultivated an international network of patronage by awarding USD 130.3 million to individuals and groups involved in international lobbying against the sanctions.<sup>38</sup>



Despite the controversies, it is worth noting that the scope of corruption associated with OFF was limited: the percentage of illicit income, kickbacks, and bribes paid through this programme formed only 2.9 percent of the total revenues sold under OFF.<sup>39</sup> This income was only 1 tenth of the money generated through smuggling schemes during the sanctions regime.

#### **iv. Smuggling**

Smuggling operations in Iraq lasted throughout the period of the sanctions and took multiple forms. The most systematic form was through bilateral trade agreements between Iraq and its neighbors Jordan, Syria, Egypt, and Turkey. Those were known as “trade protocols,” under which Iraq exported oil in return for goods and in some cases a smaller percentage of cash. By the end of the sanctions those protocols had generated the total value of USD 10 billion in goods and cash.<sup>40 41</sup> Turkey, Syria, and Jordan had applied for an exemption from the sanctions under Article 50 of the UN Charter, which allows for such an exemption if the applying country was considered by the Security Council to face “special economic problems” as a result of adhering to the implementation of UNSC-imposed sanctions. The 661 Committee “took note” of Jordan’s continuing oil imports from Iraq without approving nor prohibiting its trade with Iraq.<sup>42</sup> Syria, and Turkey were expressly denied their requests.<sup>43</sup>

Border smuggling also occurred outside these agreements through land and sea. Information regarding those activities is sporadic and anecdotal suggesting that oil and other goods (such as dates and alcohol) were smuggled for cash and goods at the Iranian, Jordanian, Syrian, Kuwaiti and Turkish borders. The only reliable estimate regarding the volume of this trade is based on SOMO’s extensive book keeping records of oil trade. Based on those records, between 1997 and 2003 Iraq generated USD 1.03 billion in border trade.<sup>44</sup>

As pointed out by Joseph Sassoon, and Joy Gordon, the smuggling and OFF illicit payments combined (between USD 10 and 12 billion), “could not have significantly restored an economy reeling from \$200 billion in damage from the 1991 war and a loss of GDP on the order of \$ 40 billion per year.”<sup>45</sup>

### **VI. 2003-2017: Statebuilding, insurgency, civil war, corruption, slow recovery, and redefining the terms of control over oil**

In March 2003, the United States led an international coalition that invaded Iraq and toppled the ruling regime in what became known as the second Gulf War. The war led to the occupation of Iraq (March 2003 – June 2004). Upon the occupation of Iraq, the US initiated ambitious state-building efforts that faced multiple challenges leading to a difficult and slow process of reconstruction. State institutions, public infrastructure and consequently the economy suffered during this decade from multiple episodes of violence, management inefficiencies, allegations of corruption, and political instability. While Iraq seems to be making a recovery after decades of strenuous economic and political circumstances, a restoration of a state of normalcy and reaching its prosperous potential are yet to be achieved.

#### **i. US-led invasion: plans for re-making the economy and their challenges**

Shortly after the occupation of Iraq, the Coalition Provisional Authority (CPA) was installed and issued its first regulation in which it clarified its role as exercising, powers of government temporarily in order to provide for the effective administration of Iraq during the period of transitional administration, to restore conditions of security and stability, to create conditions in which the Iraqi people can freely determine their own political future, including by advancing efforts to restore and establish national and local institutions for representative governance and facilitating economic recovery and sustainable

reconstruction and development.<sup>46</sup>

During its 13-month tenure, the CPA issued sweeping orders that aimed at re-making Iraqi political and economic institutions into an open market democracy. These orders and regulations covered vast areas of public life from taxes to the dissolution of state and government institutions and organizations.<sup>47</sup>

The two most devastating orders were the dissolution of the armed forces and the de-Baathification of the Iraqi state institutions and organizations. The dissolution of the armed forces contributed to the state of chaos that immediately followed the occupation of Iraq due to the lack of policing capabilities of the occupying powers. Post-invasion looting is estimated to have cost USD 12 billion. It also arguable contributed to the emergence, the persistence, and spread of the Iraqi insurgency against the occupation. The immediate impact of de-Baathification was the release of 30,000 Iraqi employees from public service, among them were middle management experts in vital government ministries and bureaus (including oil, finance, economic, local governance, education, energy, and health).

The immediate effect of those policies and post-war immediate disorder led to wide-spread halt to all public services. This effect was exaggerated further by the inability of the CPA to recruit experts with sufficient experience in their fields and especially those with regional and/or Iraqi expertise, and relied mostly on a 'revolving door of diplomats.'<sup>48 49</sup>

Economically, the CPA's policies mirrored the "shock therapy" structural adjustment programs of the mid-1990s in some former Eastern European countries. Iraq's state-owned companies, except in the hydrocarbons sector, were to be privatized.<sup>50</sup> While this was hoped to strengthen the Iraqi economy, the inability to build institutional strength and efficiency and the slow reconstruction and upgrading of the national infrastructure proved to cause long term obstacle to economic growth and sustainability.

Iraq's oil production between 2003 and 2004 was below its OFF years' levels. While in 2000 Iraq produced 2613 thousand barrels per day (KBD), in 2003 it only produced 1344 KBD and 2030 KBD in 2004. Despite the lower levels of production, Iraq benefited from increasing oil prices—while the Brent crude oil price per barrel was USD 25.02 in 2002, by 2004 it was USD 38.27 per barrel.<sup>51</sup>

Economic indicators during the occupation period mostly benefited from the increased international oil prices and the aid money that was pouring into the country. These two factors have helped keep the GDP per capita on similar levels as pre-2003. In 2002, the GDP per capita was USD 3,880 (constant 2010 USD), it remained at a comparable level in 2003 (USD 3,792) despite the decreased productivity of the oil sector.<sup>52</sup>

The main source of foreign financial assistance came from the US wherein between 2003 and 2012 it provided USD 60-63 billion for the relief and reconstruction of Iraq. Of this amount, USD 53.25 billion was actually spent. The major beneficiaries of this aid in Iraq were large corporations such as Bechtel, Fluor, Raytheon and Kellogg.<sup>53</sup>

Priority in reconstruction was given to the repair and upgrade of the electricity sector—which in addition of domestic usage, is essential for medical services, industry, and the powering of the oil sector.<sup>54</sup> With the initiation of an anti-occupation insurgency in August 2003, security took priority over electricity, and continued to be the first funding priority for many years to come due to the escalating violence.<sup>55</sup>

## **ii. Violence: draining economic resources and thwarting recovery**

Soon after the March 2003 invasion, a violent insurgency erupted in August and started spreading across the country. It targeted infrastructures, contract workers, and occupation forces. This was in addition to the emergence of violent organized criminal activities. Shortly after the transfer of sovereignty from the CPA to an interim Iraqi government in June 2004, a new violent episode erupted. Between 2006 and 2007 Iraq witnessed for the first time since the foundation of the Iraqi state in 1920 an inter-communal civil war (2006-2007). In June 2014, the Islamic State (IS) militant group captured territories in northern and western Iraq. The Iraqi forces has since then made considerable success in skirting back the IS's territories, however, the economic and social consequences are continuing to this date. These episodes have delayed reconstruction efforts due to direct and indirect targeting of infrastructure and reconstruction locations, the further destruction to the infrastructure, and the shifting of resources from development and reconstruction to security enhancement efforts. As of 2015, the IS insurgency has caused loss in economic production in the territories under its control, infrastructure destruction and the disruption of trading routes. It also led to the internal displacement of 4 million Iraqis and an influx of Syrian refugees from the war in Syria—adding more pressure on the local economic resources and creating further unemployment.<sup>56</sup>

## **iii. Oil and oil controversies**

Iraq's economy continues to rely on the oil sector despite the difficulties that this sector continues to face in terms of a weakened infrastructure and the slow pace of reconstruction. Despite the lifting of the sanctions, Iraq was not able to exceed its pre-2003 production levels until 2012 when it produced 3116 KBD. This level has since then been increasing and had reached 4,465.1 KBD in 2016. At the same time, oil prices have been increasing since 2004 when a barrel of crude oil was priced at USD 38.27 and continued to increase reaching a very high price of USD 111.67 in 2012. However, the prices have since 2014 been decreasing and as of 2016 it was USD 43.73 per barrel.<sup>57</sup> According to a 2016 World Bank report, Iraq's oil production has been slower than expected due to the effect that slow reconstruction and ongoing violence have on the ability to improve storage facilities, pumping, and pipeline capacity in the south. Despite all of that, in 2015 Iraq produced 144 billion barrels, thus ranking as the second biggest oil producer in OPEC after Saudi Arabia. And it continues to have the fifth largest proven oil reserves in the world.<sup>58</sup>

Since 2003 the Iraqi political system went significant changes, leading to the creation of a federal system. Under the federal system, the Kurdish Region has its own regional government (KRG). Since the imposition of the sanctions in the 1990s, this region has enjoyed relative economic autonomy. Under the federal system, the KRG has been in constant dispute with the central government on the mechanisms and terms on which oil resources and revenues should be managed. At the centre of these mechanisms is the Hydrocarbons law, first proposed in the Iraqi Parliament in 2007 but has since faced many objections and controversy. The law would allow foreign oil companies to have long-term contracts in Iraq and would give different regions the right to award contracts to those companies. The INOC would be restructured as an independent holding company, and a Federal Council would be created to oversee national oil policy. The law would also allocate oil revenues among the 18 governorates of Iraq based on population level.<sup>59</sup> The terms of the law, however, remain a point of dispute between KRG and Baghdad. In November 2014, the KRG and the central government reached an agreement on the mechanisms of this law as they pertain to the Kurdish region, but this agreement was suspended by mid-2015 with the KRG increasing its independent oil sales beyond the agreement, and Baghdad's transfer of oil revenue funds were lower than what was agreed upon.<sup>60</sup>

## **iv. National debt**

Iraq was able have the majority of its external debt eradicated, thus freeing the economy from one of its main burdens that had accumulated over the 1980s and 1990s. According to 2017 figures from

the Central Bank of Iraq, Iraq's total debt was USD 140 billion in 2003. After negotiations with the IMF and the Paris Club, 80 percent of this debt was cancelled except for the debt incurred from the Gulf countries (USD 45 billion).<sup>61</sup> By 2013, the total government debt was USD 73.1 billion, USD 59.3 billion of which are external debt. It is estimated that the total debt in 2016 reached USD 114.6 billion (66.7 percent of the GDP), USD 67.5 billion of which are external debt.<sup>62</sup>

#### **v. Corruption allegations and inefficiencies**

While the various episodes of violence and disorder since 2003 have had a significant impact on the reconstruction and recovery of Iraq's economy and infrastructure, allegations of corruption and management inefficiencies have also been reported as major factors in causing this delay. The spread of institutional corruption and inefficiencies has been unprecedented in the past few decades. Since the transfer of sovereignty to an Iraqi government there have been many accusations of widespread institutional corruption by local and international observers.<sup>63</sup> Iraqi institutions still suffer from corruption and inefficiencies. It still scores very poorly on the index of Transparency International corruption perception, where in 2016 it was ranked at number 166 out of 176 countries.<sup>64</sup>

#### **vi. Reforms and a slow recovery**

In 2015 demonstrations across the country demanded an end to corruption and the restoration of essential services, mainly electricity. These demonstrations were met with vast reforms at reducing governmental redundancies, inefficiencies and corruption. By the end of 2015 the six ministries were eliminated, others were consolidated and a number of senior government positions were eliminated. While these reforms are being initiated, their implementation has been slow and affected by resistance from those who are negatively affected by them.<sup>65</sup>

Iraq's recovery is still very slow and the country is still suffering from decades of compounded damage to its infrastructure during the various wars and the delays in reconstruction due to sanctions (1990s), and in post-2003 due to the poor security situation and institutional corruption and inefficiencies. According to the World Bank, as of 2015, electricity supply is rarely higher than 12 hours per day, only 50 percent of the population receive garbage collection and sewage services, and access to clean water is only 63 percent in rural areas. As a result of the government's war with IS and the influx of internal refugees and Syrian refugees, one third of the population is in need of humanitarian aid.<sup>66</sup>

Until 2017 Iraq is still considered by the World Bank as a fragile state, along with other regional countries such as Syria, Lebanon, and Yemen.<sup>67</sup> While life expectancy continued to improve regionally since the 1960s, reaching 73 years old by 2015, Iraq's life expectancy remains at its levels from the late 1990s of 69 years old.<sup>68</sup> Since 2003 the GDP per capita has never reached above the upper-middle income average as it did in parts of the 1980s and 1990s. In 2004 the GDP per capita was USD 3,782 (constant 2010 USD), and in 2015 it was USD 5,686 (constant 2010 USD).<sup>69</sup>

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<sup>1</sup> (Batatu, 8).

<sup>2</sup> Batatu vol1. Chapters 1, 2.

<sup>3</sup> Batatu (??), Slugletts (pp. 3-13), for these tradings and their routs since the late Ottoman period through the period of the monarchy see Batatu ch. 9.

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- <sup>4</sup> (Sluglett 3)
- <sup>5</sup> (Sluglett 4-5, Batatu ???)
- <sup>6</sup> (see Batatu ch 6 on this whole issue, Sluglett 31-35)
- <sup>7</sup> (Batatu 132, Sluglett 33).
- <sup>8</sup> (Batatu 32)
- <sup>9</sup> (Batatu 33)
- <sup>10</sup> (Batatu, 270)
- <sup>11</sup> (Batatu 34; 106-7)
- <sup>12</sup> (Batatu 106-7)
- <sup>13</sup> (Batatu 270; Sluglett 35-37)
- <sup>14</sup> (Yergin, ch. 10, pg 289). Daniel Yergin 1991, *The Prize: The epic quest for oil, money, and power*. Simon & Schuster: New York
- <sup>15</sup> (Yergin, 204)
- <sup>16</sup> (previous encyclopedia entry pg 480; CIA 2004: [https://www.cia.gov/library/reports/general-reports-1/iraq\\_wmd\\_2004/chap2\\_annxD.html](https://www.cia.gov/library/reports/general-reports-1/iraq_wmd_2004/chap2_annxD.html)).
- <sup>17</sup> (Batatu 959; 1033).
- <sup>18</sup> (Yergin, 646) (on the nationalization in Iraq see Batatu 1097, Yergin 584).
- <sup>19</sup> <http://data.worldbank.org/indicator/NY.GDP.PETR.RT.ZS?locations=IQ>
- <sup>20</sup> (Batatu 1097)
- <sup>21</sup> World Bank:  
<http://data.worldbank.org/indicator/SP.DYN.LE00.IN?contextual=aggregate&locations=IQ>
- <sup>22</sup> CIA 2004, [https://www.cia.gov/library/reports/general-reports-1/iraq\\_wmd\\_2004/chap2\\_annxD.html](https://www.cia.gov/library/reports/general-reports-1/iraq_wmd_2004/chap2_annxD.html)
- <sup>23</sup> See Abbas Alnasrawi 1986, "Economic Consequences of the Iraq-Iran War", *Third World Quarterly*, 8:3, pp. 869-895.
- <sup>24</sup>  
<http://data.worldbank.org/indicator/NY.GDP.PCAP.KD?contextual=aggregate&locations=IQ>
- <sup>25</sup> (CIA 2004) [https://www.cia.gov/library/reports/general-reports-1/iraq\\_wmd\\_2004/chap2\\_annxD.html](https://www.cia.gov/library/reports/general-reports-1/iraq_wmd_2004/chap2_annxD.html)
- <sup>26</sup> (CIA 2004). [https://www.cia.gov/library/reports/general-reports-1/iraq\\_wmd\\_2004/chap2\\_annxD.html](https://www.cia.gov/library/reports/general-reports-1/iraq_wmd_2004/chap2_annxD.html)
- <sup>27</sup> See Kiren Chaudhry, "Economic Liberalization and the Lineages of the Rentier State," *Comparative Politics* 27/3 (October 1994).
- <sup>28</sup> (ft. 27. Pg 8. Ntina Tzouvala. 2016 (online). Food for the Global Market: The Neoliberal Reconstruction of Agriculture in Occupied Iraq (2003-2004) and the role of international law. *Global Jurist*, ISSN (Online) 1934-2640, ISSN (Print) 2194-5675, DOI: <https://doi.org/10.1515/gj-2016-0009>.
- <sup>29</sup> Quoted in Isam al-Khafaji, "State Incubation of Iraqi Capitalism," *Middle East Report* 142 (September-October 1986), p. 4.
- <sup>30</sup> my dissertation ch 3, pg 91-2
- <sup>31</sup> WHO 1996 report.  
[http://apps.who.int/iris/bitstream/10665/59845/1/WHO\\_EHA\\_96.1.pdf](http://apps.who.int/iris/bitstream/10665/59845/1/WHO_EHA_96.1.pdf)
- <sup>32</sup> Independent Inquiry Committee 2005a, 9 FULL CITATION IN DISSERTATION CH. 5
- <sup>33</sup> Previous encyclopedia entry pg 479
- <sup>34</sup> CIA 2004 [https://www.cia.gov/library/reports/general-reports-1/iraq\\_wmd\\_2004/chap2\\_annxD.html](https://www.cia.gov/library/reports/general-reports-1/iraq_wmd_2004/chap2_annxD.html)
- <sup>35</sup>  
<http://data.worldbank.org/indicator/NY.GDP.PCAP.KD?contextual=aggregate&locations=IQ-XP>

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<sup>36</sup> world bank:

<http://data.worldbank.org/indicator/SP.DYN.LE00.IN?contextual=aggregate&locations=IQ>

<sup>37</sup> CIA 2004

<sup>38</sup> The kickback policy developed in mid-1999 when Iraq started collecting “transportation-fees” from providers of humanitarian goods as a way to recover the costs of transporting those goods from the port of Umm Qasr in the Gulf to distribution centers inside the country. By mid-2000 the policy became more institutionalized and systematic when the government imposed the “after-sales-service” fee in addition to the “transportation fee.” The new fee was imposed on all humanitarian goods regardless whether or not they were delivered by the providers to Umm Qasr or inland and it amounted to the value of 10% of each contract. It is estimated that 2,200 companies contributed to paying those kickbacks. For details on the mechanism for collecting those fees see: (Independent Inquiry Committee 2005a, Ch. 3). The biggest company involved in those purchases was the Australian Wheat Board, its role in the kickback scheme is documented in an Australian Government investigation report (Commonwealth of Australia 2006).

<sup>39</sup> My calculation based on Independent Inquiry Committee’s figures, discussed later in the text. Total oil revenues: \$64.2 billion; kickbacks on humanitarian goods: \$1.5 billion; illicit income from oil contracts: \$229 million; bribes through oil allocations: \$130 million.

<sup>40</sup> (Independent Inquiry Committee 2005e, ch.4, Iraq Survey Group 2004, 24-28) FROM CH 5 My dissertation

<sup>41</sup> This was the sum of \$5,976 million from sales to Jordan, \$3,132 million from Syria, \$2,814 million from Turkey and \$45 million from Egypt. They Egyptian agreement lasted for less than a year between late 2001 and early 2002. All other agreements lasted until the US invasion in 2003 (Independent Inquiry Committee 2005d, 97)

<sup>42</sup> (Independent Inquiry Committee 2005e, 190-210; Iraq Survey Group 2004, 24)

<sup>43</sup> Independent Inquiry Committee 2005e, 229-233; 239

<sup>44</sup> Independent Inquiry Committee 2005e, 97

<sup>45</sup> Gordon as cited in Sassoon, pg 18. Joseph Sassoon 2016. Iraq’s Political Economy Post 2003: From transition to corruption. *International Journal of Contemporary Iraqi Studies* 10:1&2, pp.17-33.

<sup>46</sup> Coalition Provisional Authority’s Regulation 1, Section 1. See CPA website,

[http://www.iraqcoalition.org/regulations/20030516\\_CPAREG\\_1\\_The\\_Coalition\\_Provisional\\_Authority\\_.pdf](http://www.iraqcoalition.org/regulations/20030516_CPAREG_1_The_Coalition_Provisional_Authority_.pdf) (accessed May 17, 2016).

<sup>47</sup> See CPA website, <http://www.iraqcoalition.org> for full list and texts of all CPA orders and regulations (accessed May 17, 2016).

<sup>48</sup> Sassoon 19-20

<sup>49</sup> examples of this are documented in many memoirs of CPA officials. For example, the book “Prince of the Marshes”

<sup>50</sup> previous entry pg 477

<sup>51</sup> BP statistics: [http://tools.bp.com/energy-charting-tool.aspx?\\_ga=2.94460828.1873435155.1505048001-1350255092.1505048001#/st/oil/region/NOA/SCA/EU/MIE/AFR/AP/](http://tools.bp.com/energy-charting-tool.aspx?_ga=2.94460828.1873435155.1505048001-1350255092.1505048001#/st/oil/region/NOA/SCA/EU/MIE/AFR/AP/)

<sup>52</sup> WB statistics

<sup>53</sup> Sassoon 20-21

<sup>54</sup> my article in *Humanity*

<sup>55</sup> My article in *Humanity* and Sassoon 20-21

<sup>56</sup> WB report, pg 13. Iraq Economic Monitor. Labouring Through The Crisis. Spring 2016.

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<sup>57</sup> BP statistics

<sup>58</sup> WB report,. Iraq Economic Monitor. Labouring Through The Crisis. Spring 2016.

<sup>59</sup> Previous entry pg. 481

<sup>60</sup> WB report,. Iraq Economic Monitor. Labouring Through The Crisis. Spring 2016

<sup>61</sup> <https://www.cbi.iq/page/33>

<sup>62</sup> IMF: <https://www.imf.org/en/News/Articles/2017/08/01/pr17311-imf-executive-board-completes-second-review-of-iraq-sba-and-the-2017-article-iv-consultation>

<sup>63</sup> See for example ICG 2011 Failing Oversight: Iraq's unchecked government and Sassoon (the whole article). Also al-Ali's book

<sup>64</sup> [https://www.transparency.org/news/feature/corruption\\_perceptions\\_index\\_2016](https://www.transparency.org/news/feature/corruption_perceptions_index_2016)

<sup>65</sup> WB: Iraq Economic Monitor. Labouring Through The Crisis. Spring 2016.

<sup>66</sup> WB: Iraq Economic Monitor. Labouring Through The Crisis. Spring 2016.

<sup>67</sup> <http://www.worldbank.org/en/topic/fragilityconflictviolence/brief/harmonized-list-of-fragile-situations>

<sup>68</sup> World Bank:

<http://data.worldbank.org/indicator/SP.DYN.LE00.IN?contextual=aggregate&locations=IQ>

<sup>69</sup>

<http://data.worldbank.org/indicator/NY.GDP.PCAP.KD?contextual=aggregate&locations=IQ-XP>